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**NAVAL
POSTGRADUATE
SCHOOL**

MONTEREY, CALIFORNIA

THESIS

**ECONOMIC AND GEOPOLITICAL INTEGRATION
BETWEEN MOROCCO AND ALGERIA**

by

Hamid Sanhaji

September 2005

Thesis Advisor:
Second Reader:

Glenn Robinson
George Lober

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**ECONOMIC AND GEOPOLITICAL INTEGRATION
BETWEEN MOROCCO AND ALGERIA**

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Submitted in partial fulfillment of the
requirements for the degree of

MASTER OF SCIENCE IN DEFENSE ANALYSIS

from the

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ABSTRACT

Morocco and Algeria face a series of urgent problems that can only be properly addressed through higher levels of economic integration and political coordination. Greater integration will achieve two main goals. First, it will help both economies by boosting trade between the two countries and by preventing “political” barriers from undermining economic exchange. Second, higher levels of political coordination will allow both countries to align their geopolitical interests in the region and avoid antagonistic objectives. The success of such a project depends on the political will of the leadership to go beyond their past disagreements, on support from civil society in both countries and the type of institutional framework that is to be adopted. Most important, the success and level of integration will depend on the countries’ ability to pragmatically address the most pressing problems each country faces and to do so in a way that is consistent with European Union (EU) and U.S. interests in the region.

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TABLE OF CONTENTS

| | | |
|------------------|--|-----------|
| I. | INTRODUCTION..... | 1 |
| | A. BACKGROUND | 1 |
| | B. PURPOSE..... | 1 |
| | C. METHODOLOGY | 2 |
| | D. OVERVIEW: PAST, PRESENT, AND FUTURE CHALLENGES..... | 3 |
| II. | ECONOMIC INTEGRATION..... | 7 |
| | A. INTRODUCTION..... | 7 |
| | B. INTEGRATION BENEFITS | 9 |
| | C. TRADE BARRIERS | 13 |
| | D. TRADE OPPORTUNITIES..... | 15 |
| | E. INTEGRATION BUILDING | 20 |
| | F. GAME THEORY..... | 24 |
| III. | POLITICAL COORDINATION | 25 |
| | A. COORDINATION OBJECTIVES..... | 25 |
| | B. ESTABLISHING COORDINATION..... | 29 |
| | C. SOME OBSTACLES..... | 34 |
| | 1. Islamism | 34 |
| | 2. The Berber Minority..... | 36 |
| | 3. Political Convergence | 37 |
| | D. THE VIEW OF THE WEST..... | 38 |
| IV. | CONCLUSIONS AND RECOMMENDATIONS..... | 41 |
| | A. CONCLUSIONS..... | 41 |
| | B. RECOMMENDATIONS | 42 |
| APPENDIX. | NASH ARBITRATION (GAME THEORY)..... | 45 |
| | A. IDENTIFY THE PROBLEM: BEFORE THE FREE TRADE AGREEMENTS (FTA'S) | 45 |
| | 1. Assumptions | 46 |
| | 2. The Game | 46 |
| | a. Governments' Options | 47 |
| | b. Challengers' Options..... | 47 |
| | c. Governments vs. Challengers | 48 |
| | d. Challengers' Game..... | 49 |
| | e. Governments' Game..... | 50 |
| | f. Status Quo and Negotiation Set | 50 |
| | B. IDENTIFY THE PROBLEM: AFTER THE FREE TRADE AGREEMENTS (FTA'S) | 51 |
| | 1. Assumptions | 51 |
| | 2. The Game | 52 |
| | a. Governments' Options | 52 |

| | | |
|-----------|--|-----------|
| b. | <i>Challengers' Options</i> | 52 |
| c. | <i>Governments vs. Challengers</i> | 53 |
| d. | <i>Challengers' Game</i> | 55 |
| e. | <i>Governments' Game</i> | 55 |
| f. | <i>Status Quo and Negotiation Set</i> | 55 |
| g. | <i>Nash Arbitration</i> | 56 |
| h. | <i>Nash Arbitration Results by Geometric Method</i> | 58 |
| C. | SUMMARY | 58 |
| | LIST OF REFERENCES | 61 |
| | INITIAL DISTRIBUTION LIST | 69 |

LIST OF FIGURES

Figure 1. Magreb Intra-Regional Trade Geography in Percent (From: DPEG).. 14

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LIST OF TABLES

| | | |
|----------|---|----|
| Table 1. | Foreign Direct Investment into Maghreb Countries. 1989-1997 (millions \$) (From: World Development Indicators 1999)..... | 11 |
| Table 2. | Maghreb Countries Exports Destination (From: DPEG) | 13 |
| Table 3. | Maghreb Countries Exports Similarity (From: DPEG)..... | 14 |
| Table 4. | Revealed Comparative Advantage of Mediterranean Countries in International Trade 1992 – 1994 (From: Escribano and Jordan, 1998) | 16 |
| Table 5. | Morocco's 2003 Imports (in MDH) (From: MCE) | 17 |
| Table 6. | Morocco's 2003 Exports (in MDH) (From: MCE) | 18 |

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LIST OF ABBREVIATIONS AND ACRONYMS

| | |
|-----------|---|
| ACM: | Arab Common Market |
| AMU: | Arab Maghreb Union |
| ASEAN: | Association of South East Asian Nations |
| CAP: | Common Agricultural Policy |
| CSE: | Casablanca Stock Exchange |
| DPEG: | The General Economic Policy Division of the Moroccan Finance Ministry: (Direction de Politique Économique Générale) |
| EEC: | European Economic Community |
| EC: | European Constitution |
| EU: | European Union |
| EIU: | The Economist Intelligence Unit |
| FTA: | Free Trade Agreement |
| FDI: | Foreign Direct Investment |
| GATT: | General Agreement and Tariffs and Trade |
| GDP: | Gross Domestic Product |
| ICG: | International Crisis Group |
| IRCAM: | Royal Institute of Moroccan Amazigh Culture |
| IP: | Istiqlal Party |
| IMF: | International Monetary Fund |
| MFM: | The Moroccan Finance Ministry: (Ministère des Finances Marocain) |
| MENA: | Middle East and North Africa |
| MCE: | The Moroccan Foreign Trade Ministry: (Ministère du Commerce Extérieur) |
| MERCOSUR: | The Southern American Common Market (“Mercado Común del Sur”) |
| NAP: | Nash Arbitration Point |
| NAFTA: | The North American Free Trade Agreement |
| OECD: | Organization for Economic Co-operation and Development |

PJD: Justice and Development Party: (Partie pour la Justice et
Developpement)

SFF: Socialist Forces Front

SWOT: Strengths, Weakness, Threats and Opportunities

WCFIA: Weather Head Center for International Affairs

WTO: World Trade Organization

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I. INTRODUCTION

Free trade is at the heart of much of the dialogue between the north and south, involving issues related to development, fairness, and human rights. While free trade offers many benefits, such as job creation, economic growth, and increased competition, there are still those who feel that opening markets too quickly is not the best approach. In particular, they are concerned that rapid opening of an economy can create uncertainty and disruption, affecting employment and business practices. As advances in technology and transportation make international economic transactions fast and reliable, nations face pressure to keep pace with international changes in trade. While existing inequalities between nations can make equal trade relationships difficult, nations cannot isolate themselves from the international market. The consensus at the present time seems to be towards a single international agreement on trade, through the *World Trade Organization* (WTO)

(The International System, 2001).

A. BACKGROUND

Morocco and Algeria recovered their independence from France, respectively, in 1956 and 1962. The periods of colonialism left them poor, economically dependent and burdened with unclear and undefined borders. From this condition, each country started building its respective economy and political system. The dominant factors unifying Morocco and Algeria are religion, culture, language, and, of course, the population and geography.

The Cold War era is over, and most countries already realize they cannot cope in an increasingly complex global environment by relying on their internal resources alone. For this reason, groups are coming together around the world with the purpose of defending themselves economically.

B. PURPOSE

Morocco and Algeria also must cooperate with each other; they must face the new challenges in their respective countries, as well as that poised from outside: Globalization. Morocco and Algeria are the two largest countries and the

two most powerful states of the Maghreb. A partnership between Morocco and Algeria has the greatest potential as a driving force for dynamic economic and political development for the whole region of North Africa. This thesis examines how, beyond the crucial Southern Moroccan provinces (Sahara) dispute, these two major states of North Africa, similar in so many ways, must seek in their recent history the means of a rapprochement. However, it is not only at the level of the state, but also at that of civil society and the different political parties that such a rapprochement can and must take place.

C. METHODOLOGY

The conduct of the qualitative analysis is based on multiple and diverse sources: books, academic journals, and scholastic research that concern specifically Morocco and Algeria.

The first chapter of the thesis is a short overview of the situation in Morocco and Algeria. The second chapter attempts to show the extent to which economic integration can resolve the two countries' common problems and benefit their respective economies, and how this integration can be undertaken. We will see that Morocco and Algeria have made significant progress to tighten their macroeconomic policies and to open their economies, but more effort is needed. There is a considerable advantage when the two countries are more open to one another. The integration between the two economies is currently weak, but there may be a significant potential trade-off, provided an adaptable framework. In addition to the framework, more political coordination between the two countries is necessary to avoid disagreements that could sever their economic ties. That will be the focus of the third chapter. Greater coordination will mainly achieve two objectives. First, it will help economic integration to accelerate for both economies' benefit, and second, it will align both countries' geopolitical interests. We will see how this coordination can be accomplished, and the issues that need to be addressed if it is to succeed. Next, we will see the extent to which that integration can impact, directly and indirectly, the interests of

the great powers in the region, especially the United States and the European Union. Finally, the fourth chapter will provide some conclusions reached as well as some recommendations.

D. OVERVIEW: PAST, PRESENT, AND FUTURE CHALLENGES

Given their common origins and identity, the histories of Morocco and Algeria were often parallel, politically, economically and socially.

After the kingdom of Morocco regained its throne and independence, the government was represented by the Istiqlal party, a continuity of the political structure of the pre-protectorate era. Meanwhile, in Algeria, a violent war of independence brought a revolutionary military force to power in contrast to the past, leaving little room for political expression (Vermeren, 2004). This transition left its mark on the political and social landscape, and the country later experienced many violent events, including military coups, civil war, and a presidential assassination.

Economically after independence, the two countries followed different orientations. In Morocco, a more liberal stance was adopted, and an active agricultural policy helped develop the rural regions and limited the risk of massive urbanization. Algeria adopted a centralized economy based mainly on hydrocarbons. Attempts were made later to diversify the economy, but that proved very difficult. Algeria appears markedly different than Morocco due to the virtually unlimited opportunities it derives from its oil wealth and mineral deposits. Its economic development plans should promote rapid industrialization, the creation of essential infrastructure, and compulsory education. All these advantages might have been combined to provide the basis for a modern way of life if certain events in 1991, by the Islamic Salvation Front (FIS) and the State, had not occurred and involved the country in deep turmoil (Zineldin, 1998).

On the social level, both societies face Islamism and Berber minority claims, though expressed more violently in Algeria than in Morocco. The unemployment rate in both countries is high, partly because their educational systems are not adapted enough to labor market needs, but also because of a

lack of dynamism in both economies. Human development indicators in 2001, comprised between 0.6 and 0.74 for the Maghreb region against 0.905 for the Organization for Economic Co-operation and Development (OCDE) countries (DPEG, 2003, p. 11), show the gap. Morocco needs a growth rate of 6% to reduce unemployment and poverty (EIU, 2004a, p. 27) and to absorb the 300,000 young workers joining the labour market every year (EIU, 2004a, p. 34). Algeria needs to create between 260,000 and 300,000 jobs just to keep the unemployment rate at the same level (EIU, 2004b, p. 30). This social situation helps Islamic fundamentalism to grow and both countries recently were hit with violence, though in different ways. The May 2003 Casablanca bombings killed forty four people including twelve of the fifteen bombers (EIU, 2004a, p. 7). In Algeria, the ban of the FIS and the intervention of the army to stop the electoral process in 1991 sparked a civil war that killed 100,000 people (Stora and Ellyas, 1999). Regional tensions are another source of conflict with the government. For example, the Berber-speaking Kabylia region in Algeria witnessed violent claims in 2001 that killed eighty people (EIU, 2004b, p. 10). This brief overview gives a picture of the social situation in both countries and shows how daunting the tasks they face truly are in their efforts to reduce poverty and unemployment and provide social peace.

Article III of the would-be European constitution states that “The union aims to promote peace, its values and the well-being of its people” (EC, 2005). This article could be a foundation for the future of Morocco and Algeria, if their relations were warmer. Their borders were closed because of territorial conflicts and security concerns, among other reasons. The Arab Maghreb Union (AMU), created in 1989, offered Morocco and Algeria a chance to settle their long-standing dispute over the Moroccan Sahara, and to create a regional common market in the Maghreb region. After some initial success, the AMU’s inability to resolve bilateral problems led to its long-term failure.

In this paper, we will argue that the economic integration can help boost Morocco and Algeria's economies and answer their common problems. It is a viable option and conceivable solution, creating socio-economic and real geopolitical conditions on which the AMU could depend for the foreseeable future.

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II. ECONOMIC INTEGRATION

A. INTRODUCTION

Since the independence of Morocco in 1956, and of Algeria in 1962, both countries have followed quite different economic policy paths. Their policies were chosen according to ideological convictions and geographical facts. Morocco actively developed its agricultural sector with the construction of more than seventy dams, mostly designated for irrigation. Despite a diversification of the economy, with the services sector representing 45% of the GDP in 2002 and 25% of the labor force and the manufacturing sector representing 18% of the GDP (EIU, 2004a, p. 26), the Moroccan economy still depends significantly on tourism and textile exports. The agricultural sector employs 43% of the labour force, and it continues to influence the domestic demand (EIU, 2004a, p. 26).

In contrast, Algeria turned its back to agriculture after independence and the Boumedienne regime stressed industries (Stora and Ellyas, 1999). The hydrocarbons sector accounts for more than 30% of the GDP and 96% of exports (EIU, 2004b, p. 29) making the economy very sensitive to hydrocarbons' price volatility. The agriculture sector accounts for 10-11% of GDP in an average year and employs 15% of the labor force (EIU, 2004b, p. 29).

Another difference between the two economies is the role the private sector plays. The privatization program launched in Morocco in 1993 has identified 114 state enterprises, around half of which have been sold (EIU, 2004a, p. 31), generating about US\$ 6 billion (MFM, 2004, p. 9).

The banking sector was reformed and opened to foreign capital, and many efforts were made to make the Casablanca Stock Exchange more attractive. Its general index rose by 25% in 2003 (EIU, 2004a, p. 46), and its capitalization was about US\$ 23 billion by the end of 2004 (CSE, 2004). These efforts were undertaken in order to inject more private capital into the Moroccan economy.

The private sector is less developed in Algeria. According to the International Monetary Fund (IMF), ill-defined land-and-real-estate property rights, an inefficient payments system, and lengthy judicial procedures are at the heart of the problem (IMF, 2004, p. 5). The Alger stock exchange remains undercapitalized, opaque, and generally unattractive (EIU, 2004b, p. 33). In 1998, a program was set up to privatize eighty-nine state-owned companies, but it failed to sell any (EIU, 2004b, p. 30).

Both countries are trying to become more integrated into the world economy. In 1996, Morocco signed a Free Trade Agreement (FTA) with the European Union, which came into operation in the year 2000. This accord is designed to lead progressively to a free-trade zone between Morocco and the EU by 2012 (EIU, 2004a, p. 27). Another FTA was signed with the United States in 2004, which will “serve as a model for further trade accords in the Middle East and North Africa” (Shelby, 2004). Algeria has not managed to emulate this FTA with the U.S. for lack of reforms, especially in the banking and the finance sectors (EIU, 2004b, p. 17). Algeria signed an association accord in 2001 with the EU to improve mainly their economic relations (EIU, 2004b. p. 18). Canada wishes to emulate the free trade agreement with Morocco, and Morocco's ambassador to Ottawa replied; “Morocco would act as an economic intermediary between Canada and African States in a ‘Triangular approach’, Morocco plays a similar role with a number of UN organisms” (“Canada should conclude,” 2005).

Decision makers in the two countries implemented economic reforms under IMF debt stabilization programs in the mid-1980s. Yet, despite significant progress toward market liberalization and stabilization since that time, the results are mixed. The growth remains below expectations; its rate between 1970 and 1999 was 1.5% in Morocco and negative in Algeria (Chabrier, 2001). It is estimated that 35% of the workforce in Algeria is either unemployed or underemployed (EIU, 2004b, p. 37) and that 18.7% of the urban workforce in Morocco is unemployed (EIU, 2004a, p. 34). In addition to the macroeconomic

and structural reforms, both countries need to boost their economies further and make them more competitive and more integrated into the world economy.

Morocco and Algeria have different policy options to achieve that objective. “They can institute policy reforms and liberalization unilaterally, following the examples of Hong Kong, China, and Singapore” (Stern, 2001). They can also opt for a bilateral approach, which has the advantage of granting both countries access to the other’s market and having reciprocal negotiations so as to protect each country’s interests and smooth the transition to a more open economy. And, finally, there is the multilateral approach chosen by the Maghreb countries in 1989 after the inauguration of the Arab Maghreb Union. The drawback of that option is that negotiations tend to be slow and cumbersome because of the number of countries involved.

We believe that one way both countries can achieve their goals and become more integrated globally is to create a regional economic zone between Morocco and Algeria. This will not only benefit their respective economies by fuelling demand, but will also give both countries the weight they need to compete worldwide. This option has a short-term cost, of course. According to the International Monetary Fund and the World Bank, when countries initiate their reform policies, there are negative economic and social effects in the short run. Giacomo Luciano said: “These effects are viewed as the price that must be paid in order to strengthen the economy over the longer term” and “the benefits accrue in the long run” (Luciano, 1995).

B. INTEGRATION BENEFITS

If there is any consensus among economists in the field of international trade, it is the proposition that free trade is almost always better than protection (“Why trade is good for,” 1998). The theory of comparative advantage ascribed to the nineteenth century British economist David Ricardo argues that “a country could gain from trade even when another country has an absolute advantage in producing all goods. The former can concentrate on producing those goods and services in which it is relatively more efficient” (Dodge, 2003, p. 2). Capital and

labor allocations are then optimally allocated and both economies gain in productivity and competitiveness.

A cross-integration of Morocco and Algeria will benefit both countries. Both economies are currently undergoing a structural change that should lead them progressively to become more integrated in the world economy. Their quasi-comparable level will allow them to smooth this transition and give them time to adapt progressively within this new economic zone. “Capital and labor re-allocation will help companies to specialize and will provoke a competition effect” (Nabli, 2002, p. 4) that will benefit them and help to build “a sound industrial base along with a solid education system, thus gaining the much needed technological independence from developed countries” (Zineldin, 1994).

This “mise à niveau” of both economies is indispensable if they are to compete with strong and well intra-integrated regional blocs such as the ASEAN and the NAFTA countries or the EU, with its market of more than four hundred million consumers and a single currency. An economic zone between Morocco and Algeria with a market of more than sixty million consumers will attract much more Foreign Direct Investment (FDI) than separate markets. There will be a “scale effect” (Nabli, 2002, p. 4) that will benefit the whole region and will fuel demand.

Morocco depends heavily on EU investments. For the period 1992 to 1995, 60.8% of the invested capital came from the EU, mainly from France, with a share of 26.2%, because of the historical ties between the two countries. The United States accounted for 12.2% only (Lahouel, 2001). If the trade barriers are removed, multinational enterprises will be attracted by economies of scale and more enticed to locate their production in the region instead of serving its markets from the EU as is the case currently. “Economists believe more integration will help to offset this “hub and spokes” in the region” (Lahouel, 2001). Some international experiences offer evidence of the positive correlation between FDI flows and regional integration. The MERCOSUR market is a successful case of south-south integration. “Bilateral trade agreements between

Brazil and Argentina signed in the 1980s evolved into a customs union that went into effect in 1995. Paraguay and Uruguay joined later. This common market received almost fourfold more capital than from the period prior to the customs union, rising to more than US\$16 billion” (Lahouel, 2001). Stuart Eizenstat, the American under-secretary of state for economic, business, and agricultural affairs stressed - when he met the finance ministers of Morocco, Algeria and Tunisia- that “The gradual reduction of intra-regional trade barriers will make the North African economies more attractive for foreign investment and more competitive at the international level” (“Sous le charme des Yankees,” 1999). The General Economic Policy Division of the Moroccan Finance Ministry (DPEG) estimates in its report that the volume of FDI in the region could reach a regular average of US\$ 3 billion a year (DPEG, 2003, p. 28), much more than the sum of potential FDI each country would receive separately. Table 1 (Martin, 2000, p. 8) shows the levels of FDI for the Maghreb countries from 1989 to 1997, with a record level of US\$ 1.5 billion in 1997. Another exceptional level of FDI was reached in 2001, thanks to the privatizations revenues in Morocco that generated US\$ 3 billion (MFM, 2004, p. 9). We can notice that the FDI is not only low on average in the region, but also very volatile from year to year.

| | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 |
|---------------|-------|------|------|------|-------|-------|------|------|-------|
| Algeria | 12.1 | 0 | 12 | 12 | 15 | 18 | 5 | 4 | 7 |
| Morocco | 167.1 | 165 | 317 | 422 | 491 | 551 | 290 | 311 | 1,200 |
| Tunisia | 79 | 76 | 126 | 526 | 562 | 432 | 264 | 238 | 316 |
| Total Maghreb | 258.2 | 241 | 455 | 960 | 1,068 | 1,001 | 559 | 553 | 1,523 |

Table 1. Foreign Direct Investment into Maghreb Countries. 1989-1997 (millions \$) (From: World Development Indicators 1999)

A larger economic zone will not only fuel demand but also diversify it. This will make the economy less vulnerable and less dependant on weather

conditions, in Morocco, for example, where agriculture influences domestic demand, or on oil prices in Algeria where hydrocarbons dominate exports.

The main trading partner of Morocco and Algeria remains the EU; the Union imports 70% and 40% of Morocco and Algeria's exports, respectively. These figures show to what extent these economies are dependent on the European activity and how narrow their negotiation latitude is with their main partner. By being more open to each other, the two economies will diversify their demand and thus be less dependent on a single partner's economic performance.

The geographical proximity of the two countries means lower transportation and communication costs, which gives them a "competitive advantage in trading with one another in developing subcontracting networks" (Holl, 2004 p. 2). Practical observation showed that countries of particular regions seem to experience growth rates that cannot be explained simply by individual countries' domestic policies. Europe in the 1950s and 1960s was a dynamic neighbourhood, mainly driven by Germany's performance. East Asia was also a good neighbourhood, thanks to the economic weight of Japan. This effect is described by economists "as the neighborhood effect and the spillovers" (Dervis, 1997). One explanation of this effect is connected to human capital and labor flows: "when a country builds a successful human capital base, members of this capital can migrate to neighbouring countries and have a positive effect on productivity (Dervis, 1997).

International experience provides evidence of the benefits of integration for learning acceleration and technological catch-up. The learning process in regional markets can be substantial. Morocco and Algeria can use the potential that exists in intra-regional trade to serve as a laboratory for developing global export competitiveness. In Latin America, "firm-level data indicate that 64 out of

106 firms participating in sampled regional trade agreements successfully made the transition from intra-regional to extra-regional exports” (Devlin and Page, 2001).

Policy emulation can be of benefit for both countries. Studies have shown that “when a country adopts a given set of policies, neighbors follow suit leading to a regional effect; and as national policies are well designed and effectively executed they are also good for regional neighbourhoods” (Dervis, 1997).

This chapter attempted to give a global picture of the many benefits of the economic integration. Despite this, trade between Morocco and Algeria remains very low and below its potential, as we will see in the next chapter.

C. TRADE BARRIERS

When we analyze trade figures in the Maghreb region, we are struck by the weakness of intra-regional trade in respect to total exports. As shown in Table 2 (DPEG, 2003, p. 18), this rate barely reached 0.6% for the period between 1996 and 2000, whereas internal trade reached 60.2% of total exports of the EU, 22.3% of the ASEAN countries, and 19.9% of those of MERCOSUR (DPEG, 2003, p. 2). Figure 1 (DPEG, 2003, p. 18) also illustrates the particular weakness of trade also between Morocco and Algeria, as shown.

| | 90 – 95 | 96 – 00 |
|--------------------------|----------------|----------------|
| All | 100 % | 100 % |
| EU | 71.90 % | 68 % |
| Maghreb | 1.10 % | 0.60 % |
| Rest of the world | 26.90 % | 31.40 % |

Table 2. Maghreb Countries Exports Destination (From: DPEG)

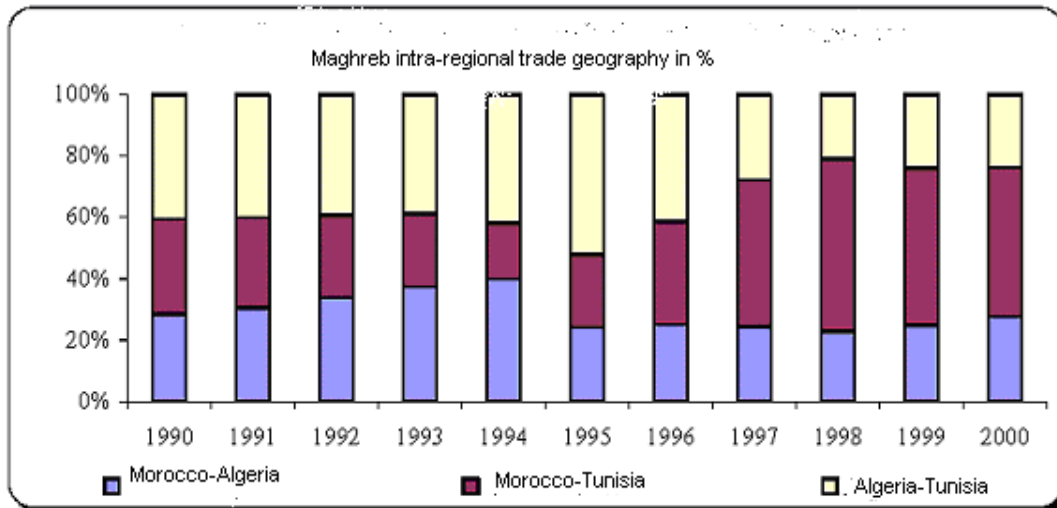


Figure 2 (Source DPEG)

Figure 1. Maghreb Intra-Regional Trade Geography in Percent (From: DPEG)

There is, paradoxically, more trade between Morocco and Tunisia, although their economies seem more similar than between Morocco and Algeria, with a lower degree of similarity. According to the DPEG, the calculation of this similarity (using the Finger-Kreinen index, which calculates the degree of similarity between exportations of two countries to the same trading partner), based on the exports to the EU, shows a level of 4.7% between Morocco and Algeria and 78.9% between Morocco and Tunisia as Table 3 (DPEG, 2003. p. 21) shows.

| | 90 – 95 | 96 – 00 |
|--------------------------|----------------|----------------|
| Morocco - Algeria | 2.50 % | 4.70 % |
| Morocco - Tunisia | 75 % | 78.90 % |
| Algeria - Tunisia | 13.70 % | 13.30 % |

Table 3. Maghreb Countries Exports Similarity (From: DPEG)

Economic models, such as the gravity models that link trade volume to the economic size and distance between partners, suggest that bilateral trade between Algeria and its neighbors is below potential (Chabrier, 2001).

The reasons for this weakness are many; besides the regional tensions and political disagreements between Morocco and Algeria that we will address later in this paper, there are many other non-tariff barriers. Transportation issues dampen intra-regional trade by increasing costs, the number of maritime lines is limited between Morocco and Algeria, the terrestrial border has been closed since the 1994 events in Marrakech, and capacity for air freight is limited (Nabli, 2002. p. 2). Finally, there are impediments in the payment system, as delays and inefficiencies seem frequent in the financial sector area (Nabli, 2002, p. 2).

These barriers prevent both economies from benefiting from their structural complementarities, but, as we will see in the next section, prospects of trade between Morocco and Algeria are promising.

D. TRADE OPPORTUNITIES

DPEG estimates trade potential in the Maghreb region to US\$ 1.6 billion, if all the barriers were removed. Morocco's exports in the region will jump from 1.6% currently to 6% of its total exports, and Algeria would reach a comparable level. As shown in Table 4 (Escribano and Jordan, 1998, p. 17), the revealed comparative advantage of Mediterranean countries shows the highest rate in mineral fuels for Algeria while Morocco remains more competitive in fruit and vegetables, clothing, agricultural products and manufacturing.

| | Manufactures | Clothing | Mineral fuels | Agricultural products | Fruits and vegetables |
|----------------|---------------------|-----------------|----------------------|------------------------------|------------------------------|
| Algeria | 0.0 | 0.0 | 9.9 | 0.1 | 0.3 |
| Morocco | 0.8 | 8.4 | 0.2 | 2.4 | 8.1 |
| Tunisia | 1.0 | 11.5 | 1.4 | 1.0 | 1.1 |
| Jordan | 0.7 | 0.6 | 0.0 | 1.6 | 5.4 |
| Egypt | 0.4 | 1.6 | 6.4 | 0.8 | 2.6 |
| Lebanon | 0.9 | 3.2 | 0.1 | 2.0 | 9.3 |
| Syria | 0.1 | 1.0 | 8.4 | 1.6 | 2.2 |
| Israel | 1.2 | 1.1 | 0.1 | 0.6 | 2.3 |
| Cyprus | 0.8 | 5.0 | 0.3 | 2.7 | 13.7 |
| Turkey | 1.0 | 7.2 | 0.2 | 2.0 | 6.6 |

Table 4. Revealed Comparative Advantage of Mediterranean Countries in International Trade 1992 – 1994 (From: Escribano and Jordan, 1998)

In the energy sector, for example, Morocco plans to increase consumption of natural gas to 5 billion cu metres/year in 2020, while local production is a mere 50 m cu metres/year (EIU, 2004a, p. 26). The country has access to 1 billion cu metres/year of Algerian natural gas, in lieu of transit fees of the Euro-Maghreb gas pipeline that crosses Morocco on its way from Algeria to Spain. Morocco could increase its import of gas from the Euro-Maghreb pipeline, but it is unlikely to want to become dependent upon this source because of the nature of its political relationship with neighboring Algeria (EIU, 2004a, p. 26). As shown in Table 5 (MCE, 2005), energy imports from Algeria represented 7% of Morocco's total energy imports in 2003 and a mere 0.5% of Algeria's energy exports in the period 1997-2000 (DPEG, 2003, p. 17).

| | All | Algeria | % |
|---|----------------|----------------|-------------|
| Food, drinks and tobacco | 11,430,387,223 | 6,879,235 | 0.0602 % |
| Energy | 21,160,546,434 | 1,510,772,274 | 7.1396 % |
| Raw materials of vegetal and animal origin | 7,324,691,576 | 3,861,400 | 0.0527 % |
| Raw materials of mineral origin | 2,473,665,319 | - | 0.0000 % |
| Semi-finished | 30,637,410,257 | 131,544,533 | 0.4294 % |
| Agricultural equipment | 1,003,985,067 | - | 0.0000 % |
| Industrial equipment | 28,968,970,839 | 31,238 | 0.0001 % |
| Consumer goods | 32,204,474,697 | 2,634,093 | 0.0082 % |

Table 5. Morocco's 2003 Imports (in MDH) (From: MCE)

Morocco's food exports to Algeria account for 0.6% of Moroccan total food exports and a mere 0.3% of Algerian food imports. Forty percent of Algerian imports come from France and Spain (DPEG, 2003, p. 17).

As shown in Table 6 (MCE, 2005), Morocco's exports of citrus and fish to Algeria are low, although Morocco has an absolute advantage in this sector and remains more competitive in comparison to its European neighbors, thanks to its developed citrus agriculture and rich fishing grounds off the Atlantic coast. The food sector illustrates the necessity for the Moroccan economy to diversify its trading partners to have more weight in bilateral negotiations. Citrus and tomatoes, which Morocco produces more cheaply than the EU (EIU, 2004a, p. 49) do not have full access to the European market and are subject to quotas imposed to protect members of the Union from the Moroccan competition.

"The Common Agricultural Policy (CAP) remains the main obstacle towards wider access by southern Mediterranean countries to European agricultural markets, where they are competitive" (Escribano, 2000).

| | All | Algeria | % |
|-----------------------|----------------|----------------|----------|
| Citrus | 2,183,963,117 | 177,600 | 0.0081% |
| Fish | 1,597,567,869 | 2,383,385 | 0.1492 % |
| Processed food | 1,304,576,777 | 20,288,219 | 1.5552 % |
| Canned fish | 3,224,989,396 | 1,954,249 | 0.0606 % |
| Clothing | 18,548,048,608 | 32,645,862 | 0.1760 % |

Table 6. Morocco's 2003 Exports (in MDH) (From: MCE)

In the fishing sector, Morocco did not renew its accord with the EU that allowed European trawlers to fish in Moroccan waters until 1999. Morocco wants to impose biological rest periods and stop over-fishing. Since the departure of the European fleet, fish exports have risen, encouraging the development of the fishing industry (EIU, 2004a, p. 38).

Algeria imports from Morocco only 0.9% of its total textile imports (DPEG, 2003). Moroccan exports of clothes to Algeria account for a mere 0.17% as shown in Table 6 (MCE, 2005). Morocco can consolidate its presence in the Algerian market, especially since the drop in its exports to the EU with the full liberalization of the sector in January 2005.

Labor mobility has served traditionally as the primary form of integration among Arab economies, and Nemat Shafik (1992) showed that the pattern of regional integration in the Middle East was unique and quite different from other examples, such as the European Union, East Asia, and North America, where trade in goods acted as the primary engine for integration, and labor movement was the final and the most controversial feature. "The migration between the countries of the region is facilitated by the similarity of culture and language" (Pissarides, 1993). Morocco and Algeria are linked not only by geographic proximity and history, common moral and religious standards, and generally

uniform modes of life, but, as well, by tradition and trading practices. "These cohesive forces help them to make good partnerships in their social and technological structures" (Zineldin, 1998)

In the tourism sector, thousands of Algerian tourists used to visit Morocco, until 1994, when an entry visa was imposed by Morocco after Algeria was alleged to be linked to Islamists who shot two Western tourists in a Marrakech hotel. Since the cancellation of the visa requirement by Morocco in July 2004, the prospect of increased Algerian tourism has risen. Prior to July 2004, most Algerian tourists, 800,000 tourists in 2002 ("Destination Tunisie," 2003), spent their holidays in neighboring Tunisia.

Capital can also flow across borders. Moroccan and Algerian businessmen can establish joint ventures wherever they can bring their local market knowledge and know-how. Once used to the neighboring market, they can invest solely in their own projects. The Casablanca Chamber of Commerce recently organised a joint economic forum, in which Algerian and Moroccan entrepreneurs worked together to establish business contacts ("Algérie-Maroc," 2005).

Algerian investors can also invest in the Moroccan exchange; the Casablanca stock exchange remains very attractive with a 25% performance in 2003. Cooperation can be developed further by merging stock exchanges, for example (Chabrier, 2001), as did the European exchanges of Amsterdam, Brussels and Paris to create the leading European Exchange: Euronext.

Morocco has also offered fiscal incentives to encourage investment in the tourism sector under the so-called "Plan Azur" (EIU, 2004a, p. 46) and is strongly promoting tourism investment. In May 2005, the United Arab Emirates drafted an accord to launch a two-billion-dollar project in the city of Rabat, which demonstrates the confidence of foreign investors in the Moroccan economy ("Morocco - UAE launch 2bn\$," 2005).

We have seen so far that trade opportunities do exist and can be exploited, provided there is an adaptable framework. The next section explains the fundamentals that both countries should address to build such a framework.

E. INTEGRATION BUILDING

The success of integration will definitely depend on the pillars on which it is built. We believe this process should be built on three fundamentals. First, the legal and institutional framework within which the economic relations will take place should be pragmatic and adaptable. Second, both economies need to be healthy to benefit fully from the integration, and thus, both countries should step up the pace of their reforms. And third, joint investments are needed to build common infrastructures to strengthen their links and facilitate cross-borders movements. The goal of these measures is to facilitate and help to correct current distortions against intra-regional trade. Economic agents will naturally come to work then to establish more links toward true integration.

The institutional framework should focus on “helping remove tariff and non-tariff barriers, while limiting bureaucratic activism” (Shafik, 1994), without imposing too many restrictions on the economies. The European Union has been less successful each time there have been interventionist policies, such as the “Common Agriculture Policy”, and technology and industrial policies.

“The regional integration can take different forms:

- It can be simply a free-trade area where both countries can grant preferential access to each other’s market.
- A customs’ union goes one step further and harmonizes custom duties for both countries vis-à-vis third countries.
- A common market is a customs union that allows free movement of factors of production.
- And, finally, an economic union extends the integration process by including policy harmonization, particularly macroeconomic and regulatory policies” (Dessus, Devlin, and Safadi, 2001).

The Algerian proposal of the Arab Maghreb Union (AMU) committees in 1989 was to build the Arab Maghrib Market in four steps. First, a free-trade zone by 1992, then a customs union by 1995, then a common market by 2000, and

finally an economic union (Ben El Hassan Alaoui, 1994, p. 164). Unfortunately, the proposal was too ambitious to be realizable.

The first step of this proposal is the most adaptable for these two countries' context (Escribano and Jordan, 1998, p. 15). Free trade agreements should be signed between the two countries on a pre-established list of products, moving gradually toward a free trade-zone agreement. The average customs duty in the region for the period from 1997 to 1999 was between 22.1% and 29.9% (DPEG, 2003, p. 23), too high a level for developing countries. In parallel to these agreements, joint commissions should be established to work on the harmonization of policies and adoption of common licensing standards in the labor market. A similar commission was established in 1990 within the AMU to work on all food security related matters (DPEG, 2003, p. 12). This general framework will be closer to the NAFTA model than to a full economic union like the EU. However, the process should be less difficult to implement in the region in comparison to North America, considering the respective market sizes. "The harmonization effort in the NAFTA area proves difficult within the sole provinces of Canada" (Dodge, 2003, p. 7), and "the Americans have different concerns with respect to the Mexican border" (Dodge, 2003, p. 6) than do Morocco and Algeria with respect to each other. The quasi-comparable level of their economies raises less concern to opening borders.

The question of whether or not to go beyond this framework toward a full single market or a monetary union is premature. The two countries need first to construct an economic zone where goods, services, capital, and labour can move freely. In the case of Europe, a single currency was a means to accelerate integration. Many European leaders believe that the euro is not only a symbol for unity but also a potential instrument to drive political integration. Joschka Fisher, once Germany's foreign minister argued in a speech in 2001 that the euro is "a profoundly political act" ("Europe's Big Idea," 2002).

The second condition for integration to succeed is the extensive reforms that must be undertaken by the two countries: "regional cooperation cannot be a

substitute for macroeconomic and structural reforms”(Chabrier, 2001).The central conclusion that emerged from a World Bank study that looked at regional trade initiatives and their successes and failures is that “most successful regional trade agreements involve either rich countries merged with other rich countries or rich countries merged with poor or intermediate countries” (Nabli, 2002, p. 5).

“Foreign Direct Investment flows are stimulated by macroeconomic stability and predictability, the quality of the infrastructure, the skills and the efficiency of bureaucracy, and the administrative procedures” (Lahouel, 2001).

Morocco and Algeria have tightened their macroeconomic policies and deregulated their markets, but further efforts are still needed. “Both countries can rely on their agreements with the EU, because those agreements provide them with a common framework for reform” (Chabrier, 2001). The IMF regrets that the state-owned commercial banks in Algeria play a quasi-fiscal role by propping up failing state-owned companies (EIU, 2004b, p. 32). The financial sector needs more reforms; “a more efficient sector with low lending margins would stimulate investment by reducing the cost of funds” (Dessus, Devlin, and Safadi, 2001. p. 41). The Credit remains expensive in Algeria and beyond the reach of most private firms and individuals, and the payment system is inefficient and unreliable (EIU, 2004b, p. 48).

In Morocco, only 20% of the financing comes from the banking sector. Moroccan manufacturing firms are financed overwhelmingly from their owners’ equity and retained earnings (EIU, 2004a, p. 44). The privatization rhythm should step up in Algeria. In 2002, the government announced that it would privatize one hundred state-owned firms. Yet by September 2004, nothing had been sold (EIU, 2004b, p. 31). The labor market needs to be regulated and harmonized to enable the work force to move freely. Morocco has adopted a new labor code designed to encourage investment and job creation and protect workers’ rights. The code formalizes the right to trade union representation and allows short-term contracts under certain conditions (EIU, 2004a, p. 29). The standards of corporate governance also should be raised in both countries, to create a

business friendly environment. Agreements on professional and technical services can promote investment and technology transfer. “The increasing pressure from both skill-intensive and capital-intensive East Asian economies and the increasing competition from the Central Eastern European countries which have a geographic proximity advantage can be countered by developing increasingly sophisticated service exports” (Devlin and Page, 2001).

Morocco is making considerable “efforts to reduce the public-sector burden and improve its efficiency”. A program has recently been set (2005) to offer about 30,000 civil servants a package for voluntary leave, “this program will help save about 12.5% of the GDP” (“Depart volontaire des,” 2005). The public administration accounted for 17% of the GDP in Morocco (EIU, 2004b, p. 57) even though it was never as large as Tunisia's or Egypt's. Also, Morocco is set to boost “E-government”, which is now to develop information online. However, the government wants it to be more than this and to offer services online. Around \$166 million was allocated to provide over two hundred services online in relation to the public sector (“Morocco set to boost,” 2005). Algeria can take an example from the Moroccan experience to reduce its administration budget and improve its efficiency.

Finally, the third pillar to help integration is the development of infrastructures and communications between Morocco and Algeria. High freight rates affect trade. Transportation laws have traditionally affected the flow of goods and capital. Surveys estimated that costs incurred by restrictive transport practices in the Maghrib “amount to US\$ 30 million for Morocco, US\$ 94 million for Algeria, and US\$ 71 million for Tunisia” (Devlin and Page, 2001). Telecommunications should be developed further. The limited number of maritime and terrestrial links results in further costs to trade and affects competitiveness. “Better infrastructures can facilitate business activities and reduce transport costs” (Holl, 2004, p. 17).

F. GAME THEORY

In addition to these three pillars, game theory also supports cooperation as the best strategy. The Appendix contains a detailed argument on Nash Arbitration Theory. In brief, it shows that the optimal solution, in the face of the internal socio-economic challenges and the new world economic order, is economic Integration between the two countries, and free trade agreements with others blocs. The two countries cannot benefit by unilaterally departing from their associate strategy. The theory gives many solutions on “the Pareto Optimal line” illustrating the negotiation set, where negotiated solutions may occur, but there is only one outcome which gives both countries and / or challengers better payoffs, or would give one of them a better payoff. From this point, either the governments of Morocco and Algeria, and/or the challengers can do better. It is the Nash Arbitration Point: NAP

History provides examples of successful unions: the United States, the largest federation, and the European Union, in the process of finalizing a common constitution. Morocco and Algeria have all the ingredients for a successful integration: the same religion, the same language, and the same cultural diversity.

III. POLITICAL COORDINATION

A. COORDINATION OBJECTIVES

In this chapter, we will discuss the extent to which political coordination can be a means to go beyond the problems of Morocco and Algeria. In Europe, the period of political dominance came to an end with the Second World War. In 1945, Germany was defeated, France humiliated, Britain bankrupt; and countries of central and eastern Europe had been absorbed by the Soviet empire (Rachman, 2004). The founding fathers of what is now the European Union - Jean Monnet, a French civil servant, and Robert Shuman, a French foreign minister- were convinced that the origins of conflict lay in the continental system of competing nation-states (Rachman, 2004).

Arab countries did try and made some efforts towards cooperation and integration, but little progress was made. “The Arab League was the first to call for agreements for economic cooperation among Arab counties” (Zineldin, 1998). The politicians did not pay enough attention to economic integration. Business and commerce were things that politicians looked down on, and thus it has never been on their agenda. Today, the importance of the national economies’ role in realizing political goals is essential and obvious: “with the emergence of various international blocs, the issue no longer needs to be argued” (Zineldin, 1998).

For these reasons, the objectives of Moroccan-Algerian coordination should be clearly defined. First, coordination will give the necessary impetus to economic integration between the two countries. Second, it will gradually align the geopolitical interests of both countries in the region. But, economic integration between Morocco and Algeria faces many obstacles because of the nature of the political relations between the two countries. The terrestrial border is still closed, and the cross-border climate is not business friendly. Creating an economic zone between Morocco and Algeria requires an institutional framework in which trade, labour, and capital movement all are regulated. To repeat,

political coordination would give the necessary impetus to economic development rather than hindering it. At the same time, economic integration creates a natural movement toward deep political integration. "In a single market, governments tend to favor uniformity, coherence, and coordination to avoid a patchwork of different policies" ("Our constitution for," 2000).

The second objective of more political coordination is the alignment of geopolitical interests. The Sahara is an area of disagreement between Morocco and Algeria. In 1975, King Hassan II organised the "Green March", a peaceful march of 350,000 Moroccans, to recover the Southern provinces (Sahara).

The Polisario, a separatist group claiming this territory, moved to Algeria and started a long guerrilla war against Morocco. This conflict gave Algeria an opportunity to weaken its rival Morocco and to hope for a potential access to the Atlantic (Hormat Allah, 2004, p. 103). A cease-fire was declared in 1991 under the auspices of the UN, but an acceptable agreement between the parties has proved elusive. One proposed referendum was rejected because of disagreements about who should be allowed to vote. Then the Polisario and Algeria rejected a solution granting general autonomy under Moroccan sovereignty. Finally, a solution allowing wide-spread autonomy, followed by a referendum, was rejected by Morocco, which considers its sovereignty non negotiable. The aim of this thesis is not to defend or demonstrate the legitimacy of Morocco's territories, which is historically self-evident. "In the eleventh century, under the Almoravides dynasty, a tribe originally coming from the Sahara, Moroccan territories stretched as far as the borders of Senegal (Hasbi and Serghini, 1998. p. 95). Nor is it our intention to demonstrate the legitimacy of the international accords, in particular, the Madrid tripartite accords in 1975 between Morocco, Spain, and Mauritania (Hasbi and Serghini, 1998. p. 95). We do argue, however, that whatever solution is adopted, it should respect Moroccan sovereignty.

Hormat Allah has presented an interesting option to resolving this conflict between Morocco and Algeria. He suggested the creation of a common

economic zone in this rich hydrocarbon and mineral region that would benefit both countries (Hormat Allah, 2004, p. 195). For Morocco, this option would end a long-lasting conflict with its neighbor and will allow the organization of a referendum by which all voters would be allowed to vote (Hormat Allah, 2004, p. 198). This would also end the inhuman detention conditions of the 408 Moroccan prisoners of war still held by the Polisario Front in the Algerian territory of Tindouf. Many have been incarcerated for over two decades and are the longest serving prisoners of war in the world, despite a U.N Security Council resolution “urging the Polisario Front to release without delays all remaining prisoners of war in compliance with international humanitarian law” (“Will somebody notices,” 2005). The Washington Times recently called for “applying the same treatment reserved to terrorist organizations to the Polisario Front. As long as it continues to hold human beings in bondage, it must be regarded as an enemy of civilization” (“Will Somebody Notice,” 2005). For Algeria, the solution to this problem will provide an opportunity to normalize its relations and develop economic cooperation with Morocco. Algeria can use the Moroccan territories to access the Atlantic and export its natural resources (Hormat Allah, 2004, p. 205). This newly opened corridor would boost the economy of the whole south-Algerian region.

This option seems a singular viable solution: it serves not only the mutual interests of Morocco and Algeria but also the United States, which has a particular interest in the region. A developed transatlantic economic zone would become more accessible and exploitable. However, the success of this solution requires a shift in the way both countries perceive the conflict. Algeria has always considered Morocco, and particularly the Sahara conflict, as an internal political “enjeu”. Instead, it would see Morocco as a committed partner for economic development in the region. Algeria should begin to consolidate its relations with Morocco and maintain a consistent attitude toward the Sahara issue. The recent declarations by Algerian President Bouteflika, including his message of support on the anniversary of the Polisario creation, coincided with the maneuvers

conducted by Polisario behind the security wall ("Polisario threatens," 2005) and exacerbated relations with Morocco. Some observers believe there is a link between the events that recently disrupted the public order in the southern city of Laayoune and the new crisis in the Algerian-Moroccan relations following President Bouteflika's declarations ("Polisario threatens," 2005). Moreover, the Algerian populace does not consider the Sahara conflict as either an internal or a national matter, but rather as a circumscribed military issue (Stora, 2002. p. 141). Houcine Ait Ahmed, leader of Algerian Socialist Forces Front (SFF), said: "If Morocco and Algeria manage to create an economic zone at their borders and If Algeria and Tunisia succeed in doing the same, the borders issue will become quite futile." He added, "Our two peoples (Moroccan and Algerian) are not doomed to receive hostile discourses and accusations that false nationalism stands for historical reality", a clear allusion to divergences between Morocco and Algeria over this latter's support for the Polisario separatists ("Creation of Algeria-Morocco," 2005).

Separatism is not a viable option to settling this conflict. The international support for the Polisario Front is weak. The number of countries recognizing the front is seriously dropping, according to the *Jeune Afrique l'Intelligent* weekly ("Serious Drop in Number," 2005). It has fallen from 76 in 1995 to 49 at present. Even the African countries recognizing the separatist group has dropped from 34 to 22 ("Serious Drop in Number," 2005). The Moroccan minister of foreign affairs and cooperation, Mohammed Benaissa, pointed out in 2003 that creating small entities in the Sahara "would be adventurous and a dangerous precedent", because "if separatism demons are unleashed, no country would be spared until the Red Sea" ("Creating Small Entities," 2003). The French doctor of geopolitics, Aymeric Chauprade, noted also in 2003 that "drawing a parallel between the Sahara and East Timor issues is not a scientific approach". For the Sahara there has been a time-old harmony between northern and southern Morocco ("Sahara is not East Timor," 2003).

Morocco and Algeria should also seek to promote social integration in the Sahara region through the organization of cultural events. The desert Music Festival organized recently in Morocco, which gathered bands from Algeria, Niger, Mali, and Senegal ("Prince Moulay Rachid," 2005), is a good example of such promotion. Morocco has an ambitious program to develop the country's southern provinces, with a global investment of US\$ 800 million for the period 2004-2008 ("Morocco Announces Program," 2004). Projects to be carried out in southern provinces will cover several sectors, including housing and urban development (US \$188 million), fisheries (US \$177 million), water and environment (US \$256 million), and roads, ports, and infrastructures (US \$173 million).

Having discussed in this section the objectives of Moroccan-Algerian coordination, in the next part we will explore some means to reach those goals and the fundamentals coordination should respect.

B. ESTABLISHING COORDINATION

The success of Moroccan-Algerian coordination will depend on the pillars on which that integration is built. There are three main requirements: the commitment of the leadership, the cooperation of civil societies, and the adaptation of the institutional framework to both countries' situations and their relationship. If integration takes place in an adaptable environment and is given necessary impetus by the leadership, then the economic and social dynamic can evolve in a virtual circle and all three pillars will be mutually strengthened.

Let us look closer at the first pillar. There have been historical rivalries for regional leadership between the two countries. Algeria decided in the wake of its independence to play an emblematic role as the third-world movement's leader, a role that had been assumed by Egypt under Gamal Abd-Nasser. The late President Houari Boumedienne of Algeria declared once that "his country will be concerned by whatever happens in Africa from Cairo to the Cap" (Hormat Allah, 2004, p. 28). The oil crisis and rising prices of hydrocarbons gave him the means to pursue his vision. With the help of the Soviet Union, Algeria equipped itself

with a military arsenal to parallel its diplomacy. But, since the fall of the Soviet bloc and the slump in oil prices, Algeria can no longer afford its third-world-leader role. Social unrest and internal crises force its leaders to focus more on domestic policy, though Algerian leaders are still tempted to exploit the Sahara issue.

The Algerian president's recent declaration of and his support message to the Polisario Front some days before the scheduled Tripoli meeting of the Arab Maghreb Union (AMU) leaders after an interruption of eleven years, forced Morocco to pull out, and the meeting was cancelled ("Le Maroc déplore les," 2005). The AMU has failed to hold a summit since 1994, notably because of tensions between Morocco and Algeria over the Sahara issue ("Bouteflika statements," 2005). This failure illustrates the nature of the Algerian-Moroccan relations. Morocco deplores the contradictory approach of the Algerian diplomacy, especially as their relations had remarkably improved after the visit of King Mohammed VI during the last Arab League meeting in Alger in March 2005. The Algerian foreign affairs minister even talked of the warming of the bilateral relations ("Un sommet de l'UMA avant," 2005). Algeria needs to have a consistent diplomatic approach to Morocco if they are to build a strong relationship. Contradictory declarations will only undermine the long-term association of two the leaders and societies.

A second condition for the success of this mutual integration is the involvement of the civil societies and their commitment to constructing a true Maghreban society. Identity concerns are still fervent in these young countries, especially in Algeria, where colonization lasted longer and the war for independence was much more violent. But both peoples should go beyond their differences and be convinced that it is in their mutual interest to have more integrated societies. We can see the extent to which popular support is crucial in the recent EU vote for adoption of the new constitution. The outcome of the referendum held in France in May 2005 showed more support for the "No" camp among the French electorate. This support is motivated by many factors, including nationalist reflexes among some electors and growing fears of a loosely

enlarged Europe to the East among others. Some analysts believe that "No" means, the end of the EU, because it will lead to a deadlock of the constitutional building process and will shake the confidence Europeans have had so far in their community.

There is an analogy between that situation and the Maghreb, to a certain extent, although Morocco and Algeria do not have the social, cultural, and linguistic distinctions that divide the European countries. For example, the quasi-comparable level of Morocco and Algeria's economies and societies raises little concern about the preservation of their social model or immigration issues.

In Europe, rich countries such as "Germany and France have developed an elaborate welfare state that is becoming increasingly unaffordable as their populations age. With the creation of a single market and a single currency, these national characteristics can cause tensions throughout the union" (Rachman, 2004).

In Morocco and Algeria, However, both nations should recognize that there is a historical gap between the generations of the 1950s, who fought colonization together, and the current generations (Stora, 2002, p. 126). This gap must be bridged. The colonization of Algeria lasted more than a century and a half and, in Morocco about fifty years. During that period, the borders delimited the two countries and limited the movement of people and goods. Historically, there were no tensions between Morocco and Algeria. There was solidarity between the two societies on numerous occasions. The Algerians supported Moroccans of the Rif during the insurrections of 1920 (Stora, 2005); a common liberation committee of the Maghreb was established in Cairo in 1948, and fundamental links were established between leaders of the nationalist parties (Stora, 2005). After independence, as the euphoria of building a great Maghrib gradually weakened, national pride in each society rose (Stora, 2005). To allow the societies to intermix, free movement of people will of course be crucial. This

raises some security concerns to be addressed later in this paper, but both countries have taken positive steps, such as Morocco's suppression of an entry visa for Algerian nationals in July 2004.

The process of building the Maghreb also includes the transversal question of culture. Writers, painters, film makers, and academics from both societies are helping to create a common vision and are a factor of rapprochement. "Culture is usually decisive and can anticipate politics" (Stora, 2005). The building of a true civil society requires meetings between intellectuals, cultural exchanges, tourism development, and students exchange programs. The role of the media is also crucial; Moroccan and Algerian satellite channels are received across the borders. Algerian music stars are applauded in Morocco, and both publics carefully follow sporting events. More economic integration also will intensify the movement of service labor, thereby strengthening the links between the communities.

The third pillar of this integration is the institutional framework. The term "political integration" as used here can only be loosely defined. Political integration can range from simply the coordination of policies between countries to the establishment of a federal state or a federation of state-nations. The model for and the form of this integration are crucial and should be adapted to the situations in both countries. An overly ambitious project may result in inefficiency. The initial framework should give the countries the ability to achieve their common goals, thereby allowing the framework to gradually evolve as their social and economic relations strengthen and the respective interests of both countries are aligned. This model should not in anyway reduce the sovereignty of member states over their own matters. A framework based more on cooperation between member states rather than on supra-national institutions will be more adaptable to the situations of both countries. "Attempts at cooperation, alliances, and integration among Arab and Islamic countries in the last four decades were too ambitious. We find big projects at the beginning and very little or nothing was left at the end" (Zineldin, 1998). The experience of the AMU gives us some idea

of how difficult it is to find broad consensus within large unions. Size matters, especially at their inception, and there is trade-off between enlargement and deepening of the union. In the case of the EU, many of the most ardent believers in the creation of the European federation see enlargement as an unwelcome distraction; “widening and deepening are often seen as opposing courses” (Rachman, 2004).

The institutional and technical organs of the AMU that were instituted in the February 1989 Marrakech meeting, and are largely inspired by the European model, are well suited for a coordination framework between Morocco and Algeria. “The presidential council is at the core of this organization, alone able to make decisions; a joint commission is in charge of all technical issues with specialised sub-commissions in each domain; a ministerial council is in charge of preparing for the head-of-states meetings and also serves as an interface between the commission recommendations and the presidential council decisions” (Ben El Hassan Alaoui, 1994, p. 126). The commission can work on three fundamental axes: economy and infrastructures, security, and social affairs and human resources.

In regard to the economic axis, the above framework describes how economic cooperation can allow both countries to strengthen their economic integration. A specialised sub-commission can work on all financial, economic and infrastructures matters: coordinating regulations, improving the economic environment by removing trade barriers, and developing cross-border infrastructures.

In parallel to an economic zone, Morocco and Algeria should begin to build a security zone, as Europe did by building the EU. The idea of armed conflict between its member countries is unthinkable nowadays. Karl Deutsch has labelled this conceptual formation as “the security community” (“Strategic Security,” 2004). Each country commits itself to ban any activity in its territories that could harm the stability or the security of its neighbor. The foundation texts of the AMU stress this point (Ben El Hassan Alaoui, 1994, p. 162). A security

sub-commission can coordinate the efforts of both countries to achieve this goal. "Morocco and Algeria agreed to set up a cooperation task group to consider illegal immigration, terrorism, and all other issues that might threaten security, peace and stability in the two sister countries" says the joint communiqué following a meeting between King Mohammed VI and President Abdul Aziz Bouteflika, ("Morocco, Algeria Set," 2003).

Finally, the third axis of concern is the social affairs. The opening of borders can enable economic and social relations to evolve naturally. Matters relative to the free movement of people, and the right of residency and individual liberties should be treated jointly. The Schengen zone within the EU is a good example of how member states' nationals can circulate freely within such a zone. These issues can be treated by a specialized sub-commission that also takes in charge the student exchange programs and joint cultural and sporting events.

Any integration process is certainly slow and difficult, and problems can disrupt the process. The following section raises some of the fundamental questions that need to be answered.

C. SOME OBSTACLES

Algeria and Morocco handle their social and political matters quite differently. The differences are apparent in the ways Islamism, ethnic minorities, and political openness were addressed in the past, even though the two societies are now gradually converging toward a common model.

1. Islamism

One question is whether Islamism is an obstacle to a successful union between Morocco and Algeria. The answer to this question can be looked at from two perspectives. Islamism has some aspects that are common to both Algeria and Morocco, but there are also fundamental differences. In both countries, a "massive and rapid urbanisation of the society has played a key role in the Islamization process" (Stora, 2005). However, Algerian Islamists took advantage of the one party regime and declared themselves as the only successor to the National Liberation Front(NLF) after its failure to resolve social problems. In his

book *"The Agony of Algeria"* the author Martin Stone talks about the "post-Chadli crisis" describing the bloody events after the army dismissed President Chadli Benjedid in January 1992. The "eradicateurs" in the Army prevented the "conciliateurs" from seeking a political solution with the main parties, including the outlawed Islamic Salvation Front ("But why?," 1997).

In Morocco, on the other hand, Islamism evolved in a multiparty system characterising the Moroccan political landscape (Stora, 2005). This explains to a certain extent the different approaches used in dealing with that phenomenon. "While Morocco adopted an integrationist way, Algeria preferred an "eradicationist way towards Islamists" (Faria and Vasconcelos, 1996, p. 8).

Extremist Islamism is more active in Algeria and is at the heart of the internal crisis that this country has experienced since the interrupted elections of 1991, which were heading toward a victory of the Islamic Salvation Front. At first, Morocco did not react to those incidents, but following the 1994 Marrakech terrorist attack that left two tourists dead and was attributed to Algerian Islamists, Morocco imposed a visa requirement for Algerian nationals. Algeria reacted by closing the border (EIU, 2004a, p. 13). This incident shows how sensitive to terrorism bilateral relations can be. On the other hand, Morocco and Algeria also at times cooperate to fight terrorism. In 2000, both authorities neutralized two Islamist groups that were supporting each other across the border (Sonnet, 2000). One journalist ironically referred to that event as "The reconciliation of Morocco and Algeria at the expenses of Islamists." This incident shows the extent to which "cooperation between the two countries can be efficient and the common security interest they have in fighting this intangible enemy" (Lehtnin, 2004, p. 5). In July 2004, Morocco removed the visa requirement for Algerian nationals.

So the question whether Morocco should close its border with Algeria to prevent a terrorist threat is now mostly irrelevant. Terrorism has become a global threat. Moreover, Algeria has made significant efforts and is progressively succeeding to contain the internal Islamist crisis.

Another perspective to take into consideration is that of political Islamism, which is more advanced in Morocco, where the Justice and Development Party (PJD) for example won 42 seats in the 2002 legislative elections. Morocco is not a secular country; Islam is the state's religion. Islamic parties, however, as other's, have the right to express their views as long as they respect the democratic policies. King Mohammed VI stressed in an interview to a Moroccan newspaper that he “**veille**”(remains bold) with respect to individual liberties and that all political sensibilities should be allowed to have access to the political arena as long as they respect the democratic rules of the country ("Entretien de SM le Roi," 2005).The Moroccan experience with the integration of the Islamist democratic parties into the political landscape has been successful so far and can inspire the Algerian neighbor.

2. The Berber Minority

In 2004, Morocco's ministry of education and the Royal Institute of Amazigh Culture (IRCAM) introduced the Berber language into some 300 primary schools throughout Morocco for the first time ("Berber teaching In Morocco," 2004). The Christian Science Monitor contrasts countries like Switzerland that comfortably mix languages in their school systems to others such as Algeria where Imazighen (ethnic minority) were harshly repressed ("Berber Teaching in Morocco," 2004). The leaders of the Front de Libération Nationale (FLN) had created a myth of Algerian nationalism that co-opted Islam and ignored the Berbers. Now those delusions are gone, stripped away by a demographic explosion (the country has more than thirty million people) and by the failure of the state to translate petroleum revenues into decent living standards ("Was De Gaulle Pushed," 2001). In 2001, large-scale unrest broke out in the region of Kabylia, and the Algerian security forces struggled to restore calm (EIU, 2004a, p. 9). Algeria could learn from the Moroccan experience how to incorporate the Berber society.

3. Political Convergence

The question of the heterogeneity of political systems continues to be raised, but differences tend to dissipate. In 1989, a new constitution was promulgated in Algeria to end the one-party system and allow multiparties. This new constitution was revised in 1996 to establish a bicameral system (EIU, 2004a, p. 12). Morocco has had a traditional multi-party system since independence, and replaced the single-chamber system with a bicameral one in 1996 (EIU, 2004b, p. 8). Algeria is opening up gradually, and its political system will eventually be close to its Moroccan counterpart.

Beyond the institutional differences between the two countries, the most important factor of convergence is the promotion of democracy, the ability of citizens to express their views responsibly. Morocco is making significant efforts to reach sustainable human development by engaging in a process of political, economic, and social reforms, that aim at ensuring fair competition and regulating the market to avoid monopolies. The National Council of Fair Competition and other regulating bodies for telecommunications and the mass media sectors were created ("Morocco's reforms to," 2005). Other reforms are being made by the creation of administrative and commercial courts, the reinforcement of the Supreme Auditing Court, and the protection of intellectual and industrial property ("Morocco's reforms to," 2005). Morocco also adopted a new "Moudawana," the Personal Status Law, restricting polygamy, and giving women equal status and the right to initiate divorce. King Mohammed VI made this issue a priority when he asked, "How can society achieve progress while women, who represent half the nation, see their rights violated and suffer as a result of injustice, violence and marginalization?" (Rachidi, 2003). Islamist leaders say the plan is in tune with their ideas, and the PJD declared that the new plan "constitutes a substantial accomplishment for the entire Moroccan people" (Rachidi, 2003). Some voices in Algeria hail this reform and wish to have the same in their country, Louisa Hanoune, secretary general of the extreme left

Labor party said that reforms in the Moroccan family code have improved the situation of women and called for similar reforms in Algeria ("Two Algerian presidential," 2004).

Former U.S. Secretary of State Colin Powell, during the 2004 Forum for the Future meeting in Morocco, highlighted the necessity for economic and political freedoms in the region, saying they go hand in hand: " Now is not the time to argue about the pace of democratic reform or whether economic reform must precede political reform" ("Political and economic," 2004). Morocco has adopted a new labor code designed to encourage investment and job creation and protect workers' rights. The code formalizes the right to trade-union representation and allows short-term contracts under certain conditions (EIU, 2004a, p. 29).

The beginning of 2004 saw the creation in Morocco of the Equity and Reconciliation Commission, with a mission to seek out off-court settlements of past human rights violations ("Amnesty International," 2005). In an interview in 1989, King Hassan II noted that it is the evolution of Algeria toward political pluralism and liberalism that has allowed the building of the AMU (Ben El Hassan Alaoui, 1994, p.161). The harmonization of political systems will lead inevitably to the disappearance of symbolic borders between the two societies.

In this part, various problems that could arise from seeking more integration have been discussed. These issues can certainly be overcome by the political will of the leadership and the commitment of the society to converge into this model. However, the external support is important as well to help these countries achieve their objectives. This next section we will try to determine the perspective from which the West will observe this rapprochement.

D. THE VIEW OF THE WEST

It is crucial to raise the question of how the great powers will see a new regional bloc in North Africa. The EU has considerable external trade with both countries, and many Algerian and Moroccan immigrants live in Europe. Stability in North Africa is of great concern to European countries. An insecure Maghreb

represents a direct threat to Europe. France was hit in 1995 by bomb attacks attributed to Algerian Islamists ("Attentats de 1995," 2002). Immigration is also a serious matter for European countries. A prosperous Maghreb may contribute to the attenuation of the wave of immigrants. "Immigration today is an increasingly visible and explosive issue in many European nations" (Vennkamp et al., 2003), and remains a sensitive one in their societies and every day life. It affects both the balance and the politics of Europe. Social problems, an African earthquake, may spread to Europe itself. There will be many refugees, especially into France from the still heavily French-flavored Algeria. The refugees will reignite political quarrels among the European Union's ten million Muslims. This will inflame right-wing nationalists in the places where the trouble is the worst ("A Hand Grenade in Mid," 1994).

Finally, a regional bloc in North Africa could help Europe adopt a common approach in its economic relations with these countries. Spanish diplomacy tries to use the Sahara issue to its advantage by sometimes backing Morocco in its claim to the territories, and sometimes Algeria in its support for the separatists (Hormat Allah, 2004, p.119). Morocco wishes that Spain would adopt "a stand of dynamic and active neutrality for a rapid settlement of the Sahara issue," as Taieb Fassi Fihri, a Moroccan official, has said, asking the Spanish public to take into account the historical facts and renounce the stereotypes and clichés about Morocco ("Morocco Calls Spain," 2002). However, the relations have been warmer since the accession of Spain's new government, headed by Mr. Zapatero ("Entretien de SM le Roi," 2005). The recent visit of King Juan Carlos and his spouse to Morocco confirms the good relations between the two kings ("Entretien de SM le Roi," 2005).

The United States is also concerned about the Sahara conflict and is trying to find a viable solution. A stable situation in this hydrocarbons-rich region will facilitate access to its resources. Some analysts forecast that 25% of U.S. needs in hydrocarbons will come from this region in 2015 (ICG, 2005, p. 26).

Two-thirds of American's direct investments in the region go to hydrocarbons extraction (ICG, 2005, p. 26) and there is an urgent need to secure this investment.

Another source of threat is the increasing number of traffickers installed in this region with a direct link to terrorism financing (ICG, 2005, p. 26). Morocco has warned against the dangers of armed gangs in the Sahara and the perils of this region becoming a den to all kinds of traffickers in weapons and illegal immigrants' traders ("Moroccan Official Warns," 2004).

American Special Forces have been operating in the African nations bordering the Sahara desert to help them deal with Islamic terrorism. The nations involved include Morocco, Algeria, Mauritania, Tunisia, Senegal, Nigeria, Mali, Chad, and Niger. Their assistance is in the form of training and new equipment ("Counter Terrorism," 2005). "The Trans-Saharan Counter-terrorism Initiative; a new program, will be officially kicked off in June and will be funded annually at US\$ 100 million over five years ("Morocco part of the," 2005).

The option proposed earlier in this thesis, the establishment of a dynamic economic zone between Morocco and Algeria in the Sahara region, provides a joint response to all these preoccupations. It will boost the region economically and secure it, thanks to more cooperation between the two countries.

IV. CONCLUSIONS AND RECOMMENDATIONS

The relationship of the partners, as in a marriage, is a key to the success of the arrangement. It may not be a sufficient factor itself, since the successful alliance needs positive quantifiable results, but it is certainly a necessary condition. An appropriate attitude has two major components, commitment and trust (Faulkner, 1992).

A. CONCLUSIONS

The need for economic growth to ease social tensions and to promote prosperity for the two societies, of Morocco and Algeria, is clearly an urgent one. The current growth rate is not sufficient to keep up with the population growth, and thus, further expansion is needed. The prospects for both economies to become more dynamic through bilateral trade are promising, and both countries can gain from more integration. There are some obstacles, such as a lack of infrastructure and telecommunications that are hindering the expansion of trade. However, the predominant obstacle is political.

Aside from the difficulties standing in the way of Maghreban integration, one should not forget that this process is naturally slow. The European community took fifty years, in spite of the firm commitment of its leadership. Contemporary history has divided the Maghreb, but it is time for the region to adopt a common political stance, build a powerful regional bloc, and be more competitive economically.

Europe has had a long history of national rivalries and two world wars before becoming the European Union. The Middle-East and North-Africa (MENA) seems to be a much more “natural” economic neighborhood than other regions in the world (Dervis, 1997). Its countries share significant similarities, such as language, religion, and culture, and there is a near-unanimous agreement to achieve economic growth by adopting a sound macro-economic policy, changing the balance between the public sector and the private sector, and opening up the economy to foreign investment and trade. The building of an Arab economic area should be undertaken by focusing first on a committed core (Shafik, 1994). There

are considerable advantages to limiting the number of participant countries to those truly committed to the process; the European Union, for instance, started with a community of six core members, and the NAFTA began with the United States and Canada, then added Mexico.

The complementarities of endowments across the region provide a basis for enhanced development. As Mosad Zenldin said in 1998: “In an Arab common market, Sudan could be the bread basket of the Arab region, the Gulf its oil reservoir, Egypt its labor force, Syria its farm and Morocco a great market. All these were and still are known facts. But what has been missing is the plan, the determination, and the operationalization of that plan” (Zineldin, 1998).

B. RECOMMENDATIONS

The success of economic integration between Morocco and Algeria can be a driving force for more integration in North Africa and the Middle East. The two countries are aware that separately, they do not possess the resources or know-how to cope with increasingly complex global environments. That’s why there is no substitute for mutual commitment to an economic and geopolitical integration. The two countries must review their present conditions and face the socio-economic and globalization challenges with an open negotiation and a committed cooperation.

As shown in the Appendix, an application of Nash Arbitration or game theory, after a joint economic integration and the signature of free trade agreements with the European Union and the United States, the two countries can present a credible position to negotiate and/or smooth the challenges into an arbitration with end results of $(3.5/4, 3.25/4)$ with 4 being the best choice for the two countries, as well as for the challengers.

For cooperation to survive, the two countries must take into account each other's comparative advantage and prevent lateral competition between them. Among the strengths of Morocco and Algeria are: strong historical, cultural, and religious backgrounds, and the availability of capital and a skilled workforce. Integration may provide numerous opportunities and benefits. Among these are

a better chance to compete globally and the creation of incentives for Algerians and Moroccans abroad to return and invest or work in their homelands, as well as the improvement of social conditions through job creation.

Morocco and Algeria cannot expect their political and economic differences to be resolved overnight. The pace at which political reforms will proceed remains an open question; therefore, the greatest responsibility of the leadership of Morocco and Algeria is to accept the “democratic syllogism as it follows:“ first, promoting economic development; then, democracy will arise from spontaneous generation” (Escribano, 2000). It is time for both countries to open their markets, even if only in a moderated, though progressive, way. This will lower costs for the two populations and will benefit North-African countries.

Rejecting economic integration means not solving the current challenges and not improving the current conditions, insofar as the Moroccan Southern provinces are a strong element in the Algerian’s internal and external political cohesion.

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APPENDIX. NASH ARBITRATION (GAME THEORY)

Applied to
Economic Integration and Free Trade Agreements
Vs.
Globalization and socio-economic Challenges
(Model created by **Hamid Sanhaji**)

In an increasingly complex global environment, some countries have undertaken a new economic integration approach. Groups are coming together around the world for the purpose of defending themselves economically.

Morocco and Algeria must cooperate with each other. They must face the new challenges in their respective countries such as education, poverty, democratization, unemployment, economic growth, and environmental degradation, as well as the challenges of globalization: Sophisticated technologies, the spread of information, and economic competitiveness, mainly from the United States, the European community, and Far-East Asia.

It is a unique solution to form the first cell, like planting a seed, which will germinate and give birth to an operational economic region, or bloc, in North-Africa. Using game theory, we will argue that the optimal solution for Morocco and Algeria is economic integration, and the Free Trade Agreements (FTA's) with the other blocs versus the challengers.

A. IDENTIFY THE PROBLEM: BEFORE THE FREE TRADE AGREEMENTS (FTA'S)

The Moroccan and Algerian economies were built under protectionism to encourage a domestic production. Taxes are very high, and the average income for the people is low. Consumers want good-quality product and free choices among articles in the market, but they cannot buy such products because they are too expensive. Thus, smugglers and traffickers respond to those demands. The black market and socio-economic and globalization challenges rapidly have

become a phenomenon that not only seriously hampers the two economies, but also threatens the stability and security of the two states and the entire sub-region.

1. Assumptions

As a result of the two governments' harmonization, common policy, and actions taken against the black market from one part, and the solutions adopted to smooth the socio-economic and globalization challenges from the other part, the following assumptions are made to develop the matrix required to understand the outcomes of the conflict "game" between the two governments and the challengers. The two operators are assumed to behave as rational actors and accept the model mathematical outcomes that likely would happen:

Note 1: *Challengers = Socio-economic problems and Globalization.*

Note 2: *Operators = Morocco and Algeria from one side as Governments, and Challenges from the other side as Challengers*

- The challenges do not pose a threat to both economies, Moroccan and Algerian
- The challenges continue spreading
- The governments of Morocco and Algeria want to end economic protectionism
- Governments of Morocco and Algeria are committed to economic integration
- The economic sectors of both countries demand action against the black Market: for example, to lower their taxes and open their markets to the world Economy
- No political concessions are made between the two countries, and economic protectionism and high taxes on goods are maintained

2. The Game

Question: Is economic integration between Morocco and Algeria a viable strategic option for answering the socio-economic and globalization challenges that exist before the Free Trade Agreements are developed?

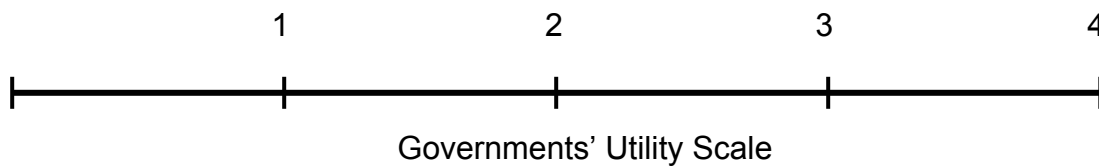
a. Governments' Options

On a scale of 4 to 1, with 4 being the best option and 1 being the worst option, this game assumes rankings for the two governments' objectives to integrate their economies.

- 4** Best Choice: Economic Integration is used; NO challenges
- 3** Next Best Choice: Economic Integration is NOT used; NO challenges
- 2** Next Choice: Economic Integration is Not used; Challengers are threatening
- 1** Worst Option: NO economic Integration; Challengers are threatening

Governments' ranking of options.

Assumption: Let us assume that the rankings as showed above, equal the cardinal utility: 4 is two times as good as 2, 3 is three times as good as 1. This assumption is necessary to conform to the Nash Arbitration.



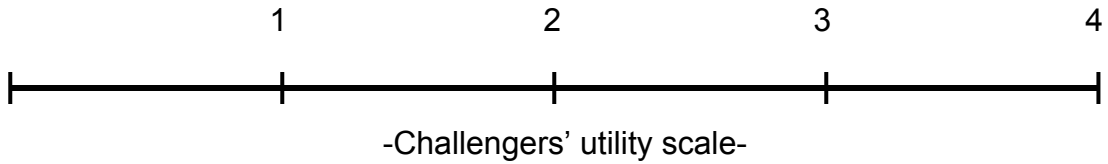
b. Challengers' Options

On a scale of 4 to 1, with 4 being the best option and 1 being the worst option, this game assumes the rankings for the challengers' objective, going higher.

- 4** Best Choice: Challenges go higher; Economic Integration used
- 3** Next Best Choice: Challenges go higher; Economic Integration NOT used
- 2** Next Choice: NO challenges; Economic Integration used
- 1** Worst Choice: NO challenges; Economic Integration NOT used

Challengers ranking of options.

The same assumption as above is made to conform to the Nash Arbitration: 4 is two times as good as 2; 3 is three times as good as 1.



c. Governments vs. Challengers

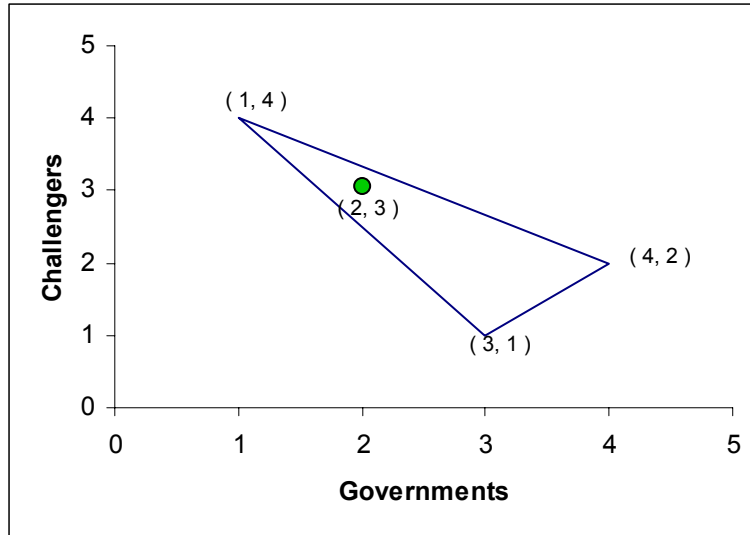
Based on the above assumptions and rankings of desired outcomes, the game develops a matrix as shown below:

| | | | |
|--------------------|----------------------|--------------------|-------------|
| | | Challengers | |
| | | Threat | No threat |
| Governments | Integration not used | <u>(2 , 3)</u> ← | (3 , 1) |
| | Integration used | ↑ (1 , 4) ← | ↓ (4 , 2) |

-Government vs. Challengers-

The expected payoffs show that a Nash equilibrium exists at **(2 , 3)**. This is to say, Governments do not use the economic integration, and the challenges continue going higher.

Note: No player can benefit by departing unilaterally from its strategy associated with an outcome: *It is the Nash Equilibrium.*



Governments vs. Challengers

No operator (governments or challengers) can benefit by departing from its associate strategy, and governments cannot threaten or promise the challengers. Then it is worth analyzing each player's game to determine if there is a possibility of improving an outcome by playing one side's game. Figures below give the results of both the governments' and challengers' games.

The objective is to show how each operator is trying to maximize its outcome while the opponent attempts to minimize the same operator's outcome: *It is the security value of each operator.*

d. Challengers' Game

| | | Challengers | |
|--------------------|----------------------|--------------------|-----------|
| | | Threat | No threat |
| Governments | Integration not used | 3 | 1 |
| | Integration used | 4 | 2 |

← Red arrows point from 'No threat' to 'Threat' for both 'Integration not used' and 'Integration used'.

↑ Green arrows point from 'Integration not used' to 'Integration used' for both 'Threat' and 'No threat'.

Challenges' goal: To maximize outcome

Governments' goal: To minimize challenges

Challengers' security value: **3**

e. **Governments' Game**

| | | Challengers | |
|--------------------|----------------------|--------------------|-----------|
| | | Threat | No threat |
| Governments | Integration not used | 2 ↑ | 3 ↓ |
| | Integration used | 1 | 4 |

Governments' goal: To maximize outcome

Challengers' goal: To minimize governments outcome

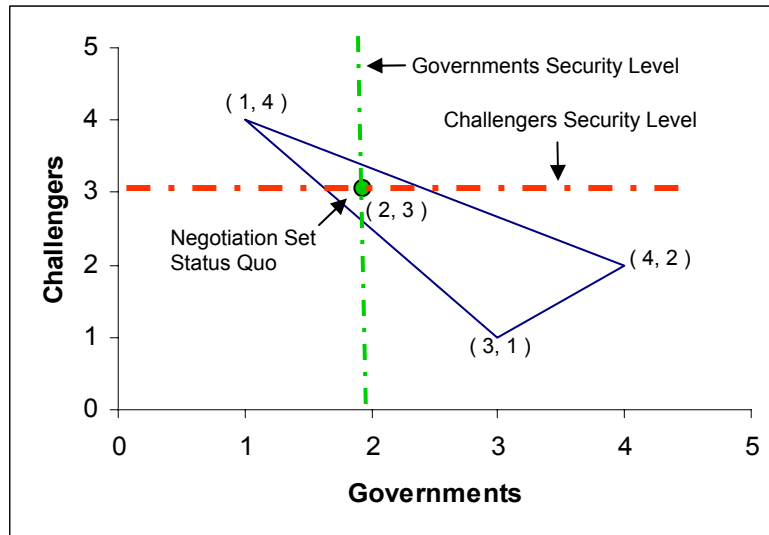
Governments' security level value: **2**

f. **Status Quo and Negotiation Set**

The Nash equilibrium (2, 3) is corresponding to the status-quo. As we will see further, the intersection of the two operators' security levels, is very close to the Pareto Optimal: this is to say, there is no better or higher payoff for both of them together or for one of them separately.

From this position, either the two governments or the challengers can improve their position. The result remains:

- Socio-economic and globalization Challenges are going higher.
- Governments are not using economic integration and free trade agreements (FTA's) to smooth and/or suppress the challenges.



Status-Quo and the Negotiation Set

B. IDENTIFY THE PROBLEM: AFTER THE FREE TRADE AGREEMENTS (FTA'S)

The governments of Morocco and Algeria, adopting economic integration, signed free trade agreements with the United States and the European Union. They will open their borders to the world market and encourage foreign development investors to come to the region. Then the problems of the black market and socio-economic and globalization challenges become crucial issues to solve by 2012, when the GATT's and WOT agreements must be implemented worldwide.

1. Assumptions

- a. The black market and socio-economic and globalization challenges are serious threats to the two countries
- b. Challenges continue spreading and hamper their economies
- c. The two countries want to stop protectionism
- d. Economic sectors of both countries demand action against the black market: For example lower taxes and open markets to the world economy
- e. Domestic economies have to be competitive

- f. Governments are willing to engage in social discussions, new employment policies to create job opportunities, and insuring economic growth

2. The Game

The same question remains: Is economic integration between Morocco and Algeria a viable strategic option for confronting the socio-economic and globalization challenges after free trade agreements have been signed?

a. Governments' Options

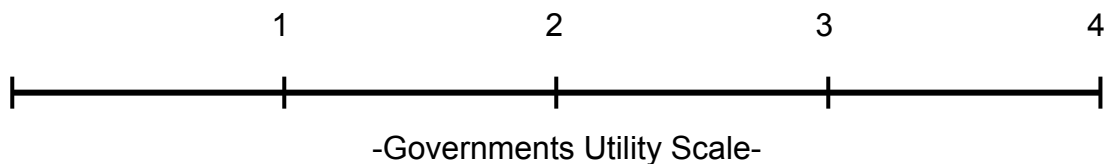
On a scale of 4 to 1, with 4 being the best outcome and 1 being the worst, let's assume the rankings for the governments' objective of integrating their economies.

Governments' Options.

- 4 Best Choice: Economic Integration Used; NO challenges
- 3 Next Best Choice: Economic Integration is NOT used; NO challenges
- 2 Next Choice: Economic Integration Used; Challengers are threatening
- 1 Worst Option: Economic Integration is NOT used; Challengers are threatening

Governments' ranking of options.

Note: To illustrate the Nash Arbitration, the upper ordinal utility of the rankings equals the cardinal utility. 4 is two times as good as 2, 3 is three times as good as 1.



b. Challengers' Options

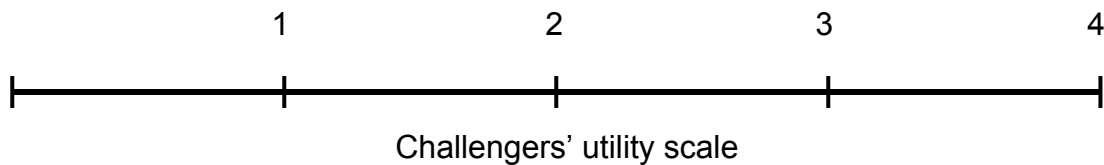
On a scale of 4 to 1, with 4 being the best option and 1 being the worst, this game assumes the ranking for challengers' objective of continuing their activities and objectives.

Challengers' Options

- 4 Best Choice: Challenges go higher; Economic Integration used
- 3 Next Best Choice: NO challenges; Economic Integration used
- 2 Next Choice: Challenges go higher; Economic Integration NOT used
- 1 Worst choice- NO challenges, and Economic integration NOT used

Challengers Ranking of Options

Note: To illustrate the Nash Arbitration, the upper ordinal utility of the rankings equals the cardinal utility: 4 is two times as good as 2; 3 is three times as good as 1.



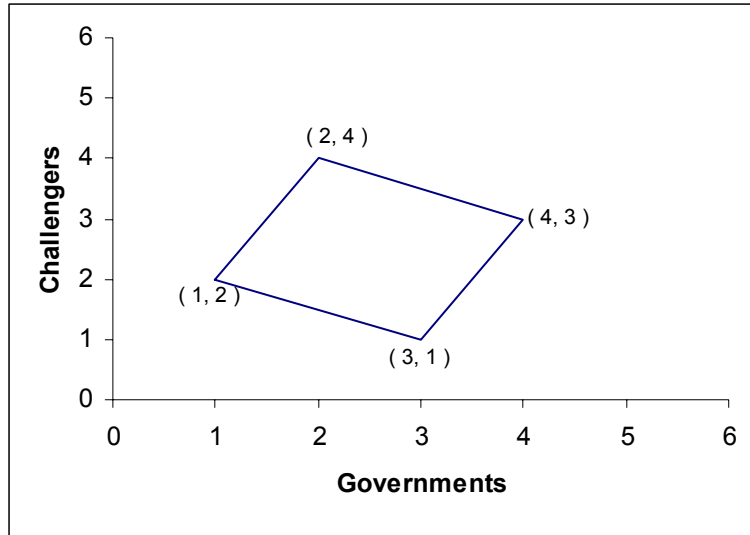
c. Governments vs. Challengers

Based on the above assumptions and rankings of desired outcomes, a game develops with the following matrix:

| | | Challengers | |
|--------------------|----------------------|--------------------|-------------|
| | | Threat | No threat |
| Governments | Integration not used | (1 , 2) ← | (3 , 1) ↓ |
| | Integration used | (2 , 4) ← | (4 , 3) ↓ |

Governments vs. Challengers

From the payoffs, it can be determined that a Nash equilibrium exists at (2 , 4): Governments are using Economic Integration, and challengers are still threatening.



Government vs. Challengers

In such a situation, in which the two operators cannot benefit by unilaterally departing from their associate strategy, it is worth determining whether governments can tackle and/or smooth the challenges.

| | | |
|----------------------|----------------------|------------------------------|
| | Challengers | |
| | Threat | No Threat |
| Integration not used | (1, 2) | (3, 1) |
| Governments | ↑ Gov. Threat | Likely threat outcome |
| Integration used | (2, 4) | (4, 3) ←.....● |

The upper figure gives the governments a good position to smooth the challenges. The governments of Morocco and Algeria will use their position of **2** (Economic Integration), and drop it to **1**, an action that forces the challengers to fall from **4** to **2**.

Given that action (Economy Integration), the challengers will rethink their game plan, choose to drop the economic hegemony and indirectly help to review the social problems in order to gain a higher outcome of **3**, by the governments not dropping the economic integration. However, and to be a credible threat, the governments must give something up in return:

- Review their economic policies for better growth
- Create job opportunities to absorb unemployment
- Open their economies to the world market

To determine the actual outcome of the game, it is worthwhile analyzing the individual player games. The following figures show the result of both the governments and the challengers. Each one is trying to maximize its outcome while the other is trying to minimize that player's outcome: *it has security value for each player.*

d. Challengers' Game

| | | Challengers | |
|--------------------|----------------------|--------------------|-----------|
| | | Threat | No threat |
| Governments | Integration not used | 2 ↑ | 1 ↑ |
| | Integration used | 4 | 3 |

Note: Red arrows point from 'No threat' to 'Threat' in both rows. Green arrows point up from the 'Threat' column values.

Challengers goal: To maximize outcome

Governments goal: To minimize challengers' outcome

Challengers' security value: **2**

e. Governments' Game

| | | Challengers | |
|--------------------|----------------------|--------------------|-----------|
| | | Threat | No threat |
| Governments | Integration not used | 1 ↓ | 3 ↓ |
| | Integration used | 2 | 4 |

Note: Red arrows point from 'No threat' to 'Threat' in both rows. Green arrows point down from the 'Threat' column values.

Governments' goal: To maximize outcome

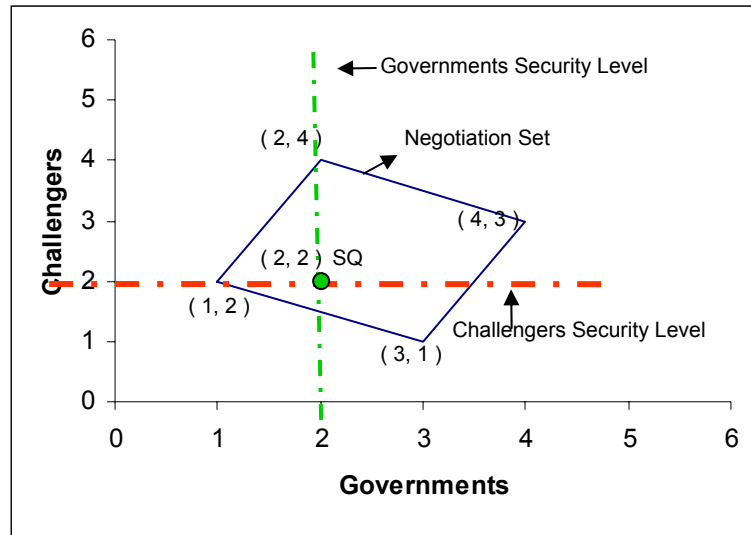
Challengers' goal: To minimize governments' outcome

Governments' Security value: **2**

f. Status Quo and Negotiation Set

The results of playing zero-sum games for both the governments and the challengers give a status quo of (2 , 2) as shown in the following figure. Challengers cannot do better than 2, but the governments of Morocco and

Algeria can improve their position from 1 – to - 2 (integration used to counter the socio-economic problems and become an economic bloc negotiator) by playing a zero sum game. The challengers will most likely view the threat position of $(1, 2)$ as the status-quo and use it, rather than the security level of $(2, 2)$, as the position from which to conduct Nash Arbitration.



g. Nash Arbitration

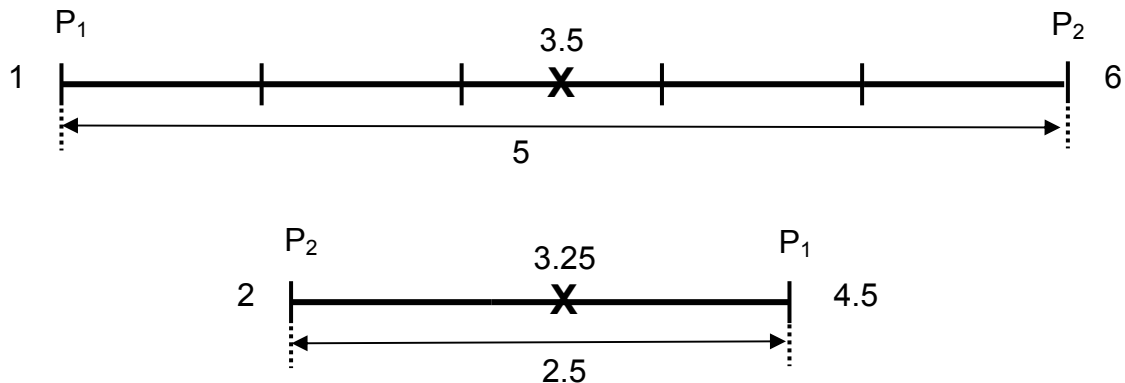
The line intersecting the points $(2, 4)$ and $(4, 3)$ is the Pareto Optimal line, illustrating the negotiation set. This is to say that there is the possibility of an outcome which gives both operators better payoffs, or would give one operator a better payoff. From this point, either the governments and/or the challengers can do better.

Arbitration from the status quo $(1, 2)$ allows the two operators to maximize their utility gains as shown in the following figure:

Using the geometric method, we can calculate the Nash arbitration position: NPA.

The extension of the Pareto Optimal line intersects with the challengers' security level at the value of $(6, 2) = P2$, and with the governments' security level at the value of $(1, 4.5) = P1$

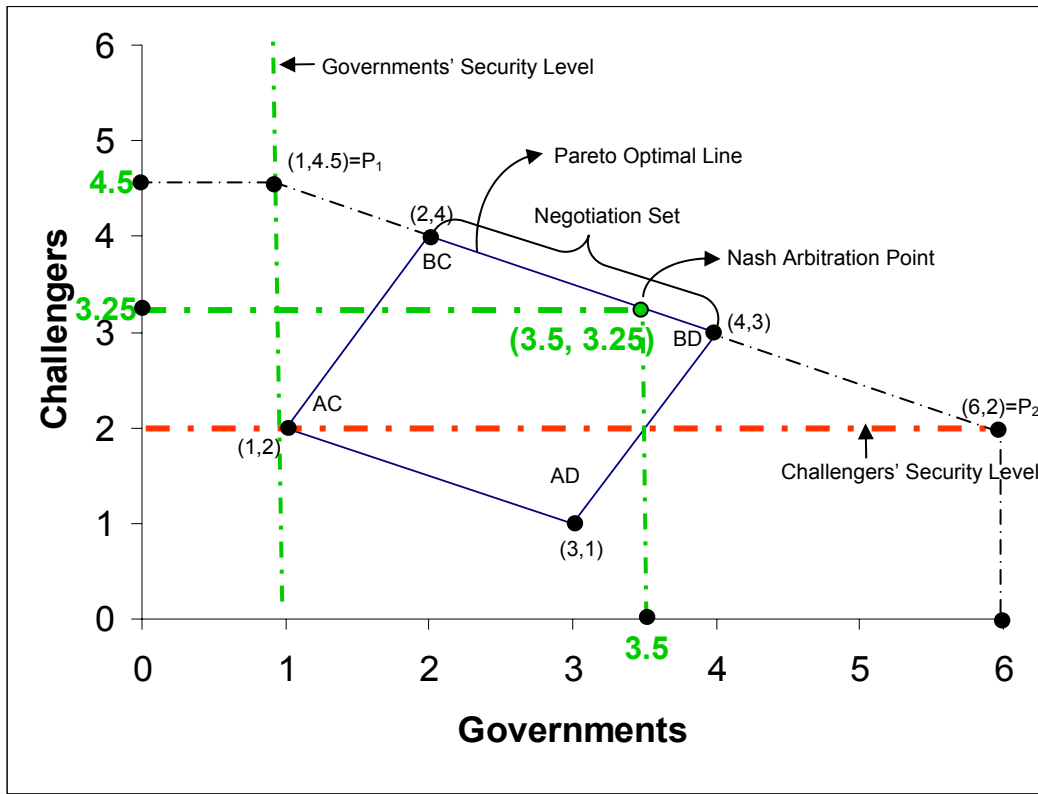
From these two positions, P1 and P2, we have the following:



By presenting a credible strategy, the governments force the challengers into an arbitration with end results of **(3.5 , 3.25)**. The challengers abandon the high position of threatening, accepting a lower outcome than the Nash equilibrium. The governments, however, must give something to the challengers:

- Create opportunity jobs to absorb unemployment
- Abandon economic protectionism and initiate the structural adjustments to allow economic growth, and adhere to the GATT and WOT regulations
- Open their economies to the world market
- Lower the taxes to encourage the domestic consumption

h. Nash Arbitration Results by Geometric Method



C. SUMMARY

Using game theory to explain the use of economic integration was not positive before the governments signed free trade agreements with the European Union, or other economic blocs for two reasons:

- The two governments used economic barriers (protectionism) and maintained high taxes on imports and law enforcement on the black market, without paying attention to the socio economic problems and populations.
- The challenges were going higher before the negotiations because:
 - The stakes were very important for both sides,
 - The operators were not rational, and
 - The FTA's were not implemented by the two countries.

After the Government of Morocco and Algeria signed free trade agreements with the European Union and the U.S, started decreasing the taxes

and opening their economies to the international market, and also promising a good socio-economic policy with the creation of job opportunities, then the challengers accepted the arbitration outcome and dropped the threats.

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